MOTION FILED

JUL 2 2 2002

(9)

No. 01-800

IN THE

Supreme Court of the United States

OCTOBER TERM, 2002

KAREN HOWSAM,

Petitioner,

v.

DEAN WITTER REYNOLDS, INC.,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE* AND BRIEF *AMICUS CURIAE* FOR THE COMPETITIVE ENTERPRISE INSTITUTE IN SUPPORT OF RESPONDENT

JAMES V. DELONG
SOLVEIG SINGLETON
COMPETITIVE ENTERPRISE INSTITUTE
1001 Connecticut Avenue N.W.
Suite 1250
Washington, DC 20036
(202) 331-1010

C. BOYDEN GRAY
Counsel of Record
WILMER, CUTLER, & PICKERING
2445 M. Street NW
Washington, DC 20037
(202) 663-6888

Counsel for Amicus Curiae

July 22, 2002

BEST AVAILABLE COPY

18 pp

MOTION OF THE COMPETITIVE ENTERPRISE INSTITUTE FOR LEAVE TO FILE A BRIEF AMICUS CURIAE IN SUPPORT OF RESPONDENT DEAN WITTER REYNOLDS[1]

The Competitive Enterprise Institute (CEI) respectfully moves this Court for leave to file the accompanying brief amicus curiae in support of respondent Dean Witter Reynolds. Consent to the filing of this brief has been received from respondent Dean Witter Reynolds (and is filed with the Clerk of this Court). However, by the time of filing we have not received a reply in response to our requests for consent from petitioner Karen Howsam.

The Competitive Enterprise Institute's interest in this case stems from the work of our scholars on the impact of regulation and litigation on the legal institution of contract.[2] The Competitive Enterprise Institute is a nonpartisan policy analysis organization founded in 1984, dedicated to the principles of limited constitutional government and free enterprise. CEI has an interest in supporting the position of the respondent, to urge that this Court enforce the intent of the parties to a contract as expressed in the plain meaning of the contract itself and the rules governing the contract. While the parties have briefed the more technical aspects of this

---

[1] Pursuant to Supreme Court Rule 37.6, *Amicus Curiae* states that no counsel for any party to this dispute authored this brief in whole or in part and no person or entity other than *Amicus Curiae* made a monetary contribution to the preparation or submission of this brief.

[2] *See, e.g.,* Comments at FTC hearing on Consumer Privacy, Julie DeFalco, July 28, 1997, at http://www.cei.org/gencon/027,01503.cfm (accessed July 16, 2002); Clyde Wayne Crews, *Antitrust Policy As Corporate Welfare,* July 1, 1997, at http://www.cei.org/gencon/025,01615.cfm (accessed July 16, 2002); Donald J. Boudreaux and Andrew N. Kleit, *How the Market Self-Polices Against Predatory Pricing*, June 1, 1996, at http://www.cei.org/gencon/025,01470.cfm (accessed July 16, 2002).

case concerning arbitration clauses, we hope that our analysis will be of help to this Court in assessing some of the broader issues the case presents concerning the interpretation of contracts.

For this reason, CEI's motion for leave to file the attached amicus brief should be granted.

Respectfully submitted,

James V. DeLong
Solveig Singleton
Competitive Enterprise Institute
1001 Connecticut Avenue N.W.
Suite 1250
Washington, DC 20036
(202) 331-1010

C. Boyden Gray
Counsel *of Record*
Wilmer, Cutler, & Pickering
2445 M. *Street NW*
Washington, DC 20037
(202) 663-6888

Counsel for Amicus Curiae

QUESTION PRESENTED

Whether arbitration contracts should be interpreted according to their terms.

TABLE OF CONTENTS

Page

QUESTION PRESENTED i

TABLE OF AUTHORITIES iii

STATEMENT OF INTEREST OF AMICUS CURIAE 1

SUMMARY OF ARGUMENT 1

ARGUMENT 2

THE COURT SHOULD LOOK TO THE TEXT OF THE CONTRACT TO DETERMINE THE INTENT OF THE PARTIES TO THE CONTRACT. 2

A. Contracts Benefit Both Parties: The Present Agreement Is No Exception 2

B. This Court Should Look to the Text of the Contract and the NASD Rules as Guide to the Parties' Intent 7

CONCLUSION 11

TABLE OF AUTHORITIES

Page(s)

Cases

E.E.O.C. v. Waffle House, Inc.,
122 S. Ct. 754 (2002) 3

Mastrobuono v. Shearson Lehman Hutton, Inc.,
514 U.S. 52 (1995) 2

Milliken v. Pratt,
125 Mass. 374 (1878) 5

PaineWebber Incorporated v. Hartmann,
921 F.2d 507 (3d Cir. 1990) 9

Pennzoil Co. v. FERC,
645 F.2d 360 (5th Cir. 1981) 9

United Van Lines, Inc. v. United States,
448 F.2d 1190 (D.C. Cir. 1971) 9

Volt Information Sciences, Inc. v. Board of Trustees of Leland Standard Junior Univ.,
489 U.S. 468 (1989) 3, 8

Constitutions and Statutes

42 U.S.C. § 1981 6

9 U.S.C. § 4 8

U.S. Const., Art. 1, § 10, cl. 1 4

Other Authorities

Bruno Leoni, *Freedom and the Law*
(1972) 5

H. Maine, *Ancient Law*
(Raymond Firth ed., Beacon Press 1963) (1861) 4

H.R. Rep. No. 96, 68th Cong., 1st Sess., 1 (1924) 2

Mark Tushnet, *Following the Rules Laid Down: A Critique of Interpretevism and Neutral Principles*,
96 Harv. L. Rev. 781 (1983) 5

Michael I. Krauss, *Tort Law and Private Ordering*,
35 St. Louis U. L.J. 623 (1991) 4

The Death of Contract (1974) 2

STATEMENT OF INTEREST OF AMICUS CURIAE

The interest of the Competitive Enterprise Institute in this case is set out in the previous motion for leave to file this amicus brief.

SUMMARY OF ARGUMENT

This case presents the question of whether the application of a time limit on the arbitrability of a dispute is the province of the arbitrator, or whether a court may apply the limit. The time limit in question is an NASD rule, incorporated in the contract between petitioner Karen Howsam and respondent Dean Witter.

We urge the Court to resolve this dispute over the meaning of a contract providing for arbitration primarily by looking to the text of the contract and the rules incorporated into it for guidance, as these parties must have, and as other parties to other similar contracts will in the future.

In the first part of our argument, we review this Court's precedents on the interpretation of arbitration contracts, which explain that the Federal Arbitration Act (FAA) was not intended to displace focus on the intent of the parties to the contract by federal statutory policy. Rather, the FAA set arbitration contracts on the same footing as other contracts. We then offer a broad perspective on the mutual benefits of contract for both contracting parties. We conclude by examining standardized contracts, sometimes called "form contracts," of the type often at issue in arbitration cases such as this one.

In the second part of our argument, we look more closely at the contested contractual and regulatory text in this case. This Court has in the past looked first and foremost to the text of arbitration contracts to resolve arbitrability disputes; in this instance, that approach should result in a ruling in favor of respondent.

ARGUMENT

THE COURT SHOULD LOOK TO THE TEXT OF THE CONTRACT TO DETERMINE THE INTENT OF THE PARTIES TO THE CONTRACT.

Viewed narrowly, this case presents the Court with the question of whether the time limitation provision of an arbitration clause is to be applied by an arbitrator or by a judge. But this case also raises larger issues of the courts' approach to the interpretation of securities arbitration contracts and, indeed, contracts in general. In the last century, some jurists anticipated the death of contract, brought about by the expansion of the law of tort.[3] This case presents the Court with an opportunity to clarify that its precedents do not require that contract be drowned in a sea of policies and presumptions divorced from the intentions of the contracting parties.

A. Contracts Benefit Both Parties: The Present Agreement Is No Exception

Respect for private parties' authority to enter into voluntary agreements motivated the passage of the Federal Arbitration Act. The Act was intended to counteract judicial decisions that disfavored arbitration and to place arbitration agreements on the same ground as other contracts. H.R. Rep. No. 96, 68th Cong., 1st Sess., 1 (1924). Consistent with this respect for the intentions of the contracting parties as embodied in their contract, this Court's precedents make it clear that, in arbitration contracts, it is the parties' intentions, not statutory or judicial policies, that govern. As the Court has explained, "the FAA's proarbitration policy does not operate without regard to the wishes of the contracting parties." *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 57 (1995). The FAA thus directs courts "to place

[3] *See* G. Gilmore, *The Death of Contract* 97-94 (1974).

arbitration agreements on equal footing with other contracts," but it "does not require parties to arbitrate when they have not agreed to do so." *E.E.O.C. v. Waffle House, Inc.*, 122 S. Ct. 754, 764 (2002), citing *Volt Information Sciences, Inc. v. Board of Trustees of Leland Standard Junior Univ.*, 489 U.S. 468, 478 (1989). Simply put, "this Court will not override the clear intent of the parties, or reach a result inconsistent with the plain text of the contract, simply because the policy favoring arbitration is implicated." *Waffle House*, 122 S. Ct. at 764.

The FAA's focus on honoring the parties' intent benefits *everyone* who enters into an arbitration contract. Contract law is a remarkable institution. It empowers almost anyone to reduce future uncertainties by creating a relationship with a stranger governed by detailed rules suited to the parties' own unique circumstances. It is an axiom of economics that both parties to a contract benefit from the relationship; otherwise, they would not have agreed to it. Each party has promised the other something that he lacked beforehand; hence, upon agreeing, each party becomes better off. These trades raise societal standards of living as a whole.[4] They

[4] Professor Michael Krauss explains:

> Contract law, to paraphrase a classic liberal paradigm, arises from man's realization that natural liberty, if unaccompanied by binding cooperation, will result in a self-sufficient life that is "solitary, poor, nasty, brutish and short." From this realization springs the deep and meaningful paradox that liberty is most meaningfully implemented when it is voluntarily traded away. Though man may not alienate his freedom entirely, he can and indeed must parcel bits of it off if he wishes to participate in a social life. By doing this, of course, he produces consumer surplus that results in wealth for his fellows while at the same time receiving from the latter more than he gives up—according to his own, freely determined function of values.

regularize relations between strangers, otherwise governed only by the bare vagaries of tort or statutory rules crafted by others.[5] Contracting enables ordinary workers to trade their work for wages and ultimately for dazzling arrays of commercial goods and services. The fundamental importance of contract to society is recognized and embodied in the Constitution's Contracts Clause, one of the few clauses from the founding era that applies directly to the states.[6]

Widespread personal freedom to enter binding agreements arose under the common law at the end of the eighteenth century. Judges began to cast aside paternalistic medieval legal concepts "protecting" certain categories of persons such as seamen by preventing them from entering into certain types of contracts, instead recognizing the mutual benefits of contract.[7] This tectonic shift in legal perspective from "status" to "contract" had broad implications for personal freedom and social advancement, as Sir Henry Maine noted long ago.[8] It is ironic that this freedom is still threatened today, often in the name of

---

Michael I. Krauss, *Tort Law and Private Ordering*, 35 St. Louis U. L.J. 623, 625-626 (1991).

[5] See Walter Olson, *Tortification of Contract Law: Displacing Consent and Agreement*, 77 Cornell L. Rev. 1043 (July, 1992) ("Tort law is modeled on the one-sided, gratuitous infliction, as when a stranger drives into your front porch and demolishes it. Nothing is pre-arranged or arrangeable; nothing is of mutual benefit...").

[6] "No State shall ... pass any ... Law impairing the Obligation of Contracts...." U.S. Const., Art. 1, § 10, cl. 1.

[7] P. S. Atiyah, "Common Law," *in The New Palgrave: A Dictionary of Economics (The Invisible Hand)* 70, 73-75 (John Eatwell, Murray Milgate, and Peter Newman, eds., 1989).

[8] See H. Maine, *Ancient Law* 165 (Raymond Firth ed., Beacon Press 1963) (1861) ("[W]e may say that the movement of the progressive societies has hitherto been a movement from Status to Contract.").

fairness, but ultimately with similar results to the old paternalism.

Should the legal system deprive certain individuals of the capacity to be able to enter binding agreements, it would do them no favor. Those individuals will soon find the universe of persons willing to contract with them on favorable terms rapidly shrinking. When Roman lawmakers decreed that it was unfair to require women to be bound by their contracts, because it was in women's nature to constantly change their minds, they quickly found merchants refused further dealings with women.[9] In our own country, "married women" statutes depriving women of the right to contract were long a mark of second-class civil status. *See, e.g., Milliken v. Pratt*, 125 Mass. 374 (1878) (seminal case enforcing a married woman's agreement and noting the tendency of modern legislation to "enlarge" women's contracting rights). The "slave codes" offer another notorious example. As Professor Mark Tushnet points out, the framers of the Fourteenth Amendment were well aware of the central importance of granting freed slaves the right to enter binding agreements. In particular, they "thought that freedom of contract was extremely important because it was the foundation of individual achievement."[10] Accordingly, after the civil war, one of the most important rights given to

---

[9] Bruno Leoni, *Freedom and the Law* 143 (1972) (describing the enactment of the *Senatus Consultum Velleianum*, noting "People had very little desire to enter into contracts with women after the enactment of the *Senatus Consultum*. A remedy for this inconvenience was finally found by admitting that women could renounce the privilege of the *Senatus Consultum* before engaging in some contracts, such as the sale of land.")

[10] Mark Tushnet, *Following the Rules Laid Down: A Critique of Interpretevism and Neutral Principles*, 96 Harv. L. Rev. 781, 801 (1983).

former slaves was the right to sue and be sued—the right to contract.[11]

Amici Curiae Trial Lawyers for Public Justice and the AARP appear to recognize these fundamental points on one level, because they argue that the parties' intentions should not be set aside in considering arbitration obligations. But they then imply that clauses concerning arbitrability should be viewed as imposed or coerced simply because a consumer or worker has signed a largely standardized contract. This argument has no application to this case because Petitioner Howsam has not hinted or alleged that this was a "contract of adhesion," or that any element of coercion or fraud entered into its making.[12]

More fundamentally, standardized contracts are beneficial for consumers, not harmful; they certainly are not inherently coercive. Standardized contracts (also called "form contracts") have emerged in the marketplace because similarly situated customers have similar needs. And all customers value their time; hardly anyone would wish to renegotiate individual items in a complex commercial contract. Nor is there need for customers to do so to protect their interests. Competition between employers for workers

---

[11] Enforcement (Klu Klux Klan) Act of 1871, 17 Stat. 13 (1871). The Act is now codified at 42 U.S.C. § 1981 ("All persons within the jurisdiction of the United States shall have the same right in every State and Territory to make and enforce contracts, to sue…").

[12]Furthermore, the theory that inequalities of bargaining power alone result in a form of "coercion" is invalid. It is coercion when a mugger points a gun at you and says, "your money or your life." When you hand over your money, you have received no benefit from the mugger; his power to take your life should not be confused with a new benefit that he confers upon you by refraining from taking it. It was never his to give. By contrast, *every* contract confers benefits on both parties. The view that arbitration clauses are "imposed" on consumers therefore has no more validity than arguing that Safeway robs us because we cannot haggle down the price of an apple.

and between businesses for customers ensures that, over time, businesses offer more favorable deals. Theories that mindlessly stigmatize standardized contracts as "contracts of adhesion" critically underestimate the fact that competition benefits consumers and employees with respect to prices paid, quality, service, and other terms. As a general rule, standardized contracts, like standardized goods, benefit consumers.

B. This Court Should Look to the Text of the Contract and the NASD Rules as Guide to the Parties' Intent

In the previous section we set out reasons this Court should affirm its rulings giving dispositive attention to the intentions of the contracting parties in cases involving arbitration clauses. Here we explain why the text of the arbitration contract at issue in this case, together with the governing NASD rules, are once again the Court's best guide.

At issue in this case is the impact of two provisions of the NASD Code of Arbitration on the arbitration clause of a contract for the sale of securities. The contract signed by petitioner Karen Howsamm contained an arbitration clause. Under that clause, when a dispute arose under the contract, petitioner Howsam elected to arbitrate before the NASD. Section 10304 of the NASD rules, "Time Limitation Upon Submission," provides, in relevant part, that "No dispute, claim, or controversy shall be eligible for submission to arbitration under this Code when six (6) years have elapsed from the occurrence or event giving rise to the act or dispute . . ." In addition, section 10324 of the rules, "Interpretation of Provisions of Code and Enforcement of Arbitrator Rulings," provides in relevant part that "The arbitrator shall be empowered to interpret and determine the applicability of all provisions under this Code and to take appropriate action to obtain compliance with any rulings by the arbitrator(s)…"

Petitioner Howsam's claims, stemming from the sale of securities in 1992, might be time barred under these provisions. This case will determine whether, under the rules, a court or the arbitrator should decide whether a time bar applies. Both parties agree that the NASD rules should be incorporated into the contract for purposes of interpreting its meaning. As explained above, when a contract providing for arbitration is clear, the Court has consistently looked to the language of the agreement, not to statutory policies or judicial presumptions, to resolve questions of interpretation. *See* pages 2-3, above.

In contrast with this case law, petitioner's brief and the brief of the SEC put forward countless judicial and statutory policies and presumptions before ever reaching the language of the agreement. The first of these rules of thumb is what petitioner misdescribes as a "strong federal policy in favor of arbitration, applicable in both state and federal courts." Brief for the Petitioner, at 10. But this Court has made it clear that the FAA "confers only the right to obtain an order directing that "arbitration proceed *in the manner provided for in [the parties'] agreement.*" *Volt*, 489 U.S. at 469 (citing 9 U.S.C. § 4, emphasis added by *Volt* Court). It far overstates the case to think of the FAA as "favoring" arbitration. Rather, as noted above, the FAA was designed to counteract judicial decisions that *dis*favored arbitration and to place arbitration agreements on the same ground as other contracts. *See* page 2 above. The text and history of the FAA thus provide no grounds for displacing an inquiry into the clear language of the contract and the interpretive rules governing it.

To be sure, the arbitration clause in this case is a general one, referring all disputes to the arbitrator. But this general provision should be read in light of the fact that *all* the potential arbitration forums contain time limitation provisions. *See* Brief for the Petitioner, p. 11. It thus seems *un*reasonable to interpret the general arbitration clause to mean that time-barred claims or the issue of their

arbitrability are to be referred to the arbitrator. The contract at issue here, like other contracts, should be interpreted in light of commercial custom. *See, e.g., Pennzoil Co. v. FERC*, 645 F.2d 360, 388 (5th Cir. 1981); *United Van Lines, Inc. v. United States*, 448 F.2d 1190, 1195 (D.C. Cir. 1971).

The SEC's brief notes that courts have ruled that, in general, time limits in arbitration clauses *outside* of the securities area are for the arbitrator to apply. *See* Brief for the SEC, p. 23. The fact that the courts have *not* agreed about securities time limitation rules, however, should be a red flag that there is something particular about the rules' customary wording in the securities context. *See, e.g., PaineWebber Incorporated v. Hartmann*, 921 F.2d 507 (3d Cir. 1990) (considering Rule 603 of the New York Stock Exchange Department of Arbitration, providing that no dispute over six years old "shall be eligible for submission to arbitration"). The NASD time limitation rule says, in simple terms, that claims over six years old are not "eligible for submission to arbitration." This language is perfectly clear and precise, far more so than the general wording of Section 10324, a generic empowering clause. When the two rules are read together, they are best reconciled by taking the view that Section 10324 only comes into play when the arbitrator's authority has been properly invoked—that is, when a claim is *not* time barred. Consistent with her contract and the NASD rules as a whole, it is hard to see how any aspect of the dispute over petitioner Howsam's claims can be submitted to the arbitrator, given that Howsam does not present any colorable argument that her claims are less than six years old.

The SEC contends at length that the time limitation rule might have been worded differently. Brief for the SEC, p. 25. This is significant. Why should the SEC argue this point, if the wording of the rules cuts in its favor? In any case, the more important fact is that the time limitation rule was *not* worded differently. The plain language of the rules as

promulgated should be enforced, as this Court has repeatedly emphasized, for it is that language that gives the parties the only firm indication as to their duties.

Petitioner's additional policy arguments only confirm that contracts should be interpreted according to the parties' expressed intent. Paragraph after paragraph of the briefs for petitioner is devoted, for example, to attempting to show that a time limitation is more "procedural" than "substantive" and should therefore be left for the arbitrator. *See, e.g.,* Brief for the SEC, 13-16. This inquiry is far from persuasive. Indeed, it is nearly incoherent to argue that a time limitation provision does not determine what "subject matter" is arbitrable. The time limitation rule pertains to the time the claim arose, specifically to the problem of the documentation and other evidence available (or not) in support of that claim after six years has passed. If a claim is stale, that is a feature of the claim itself, not a problem relating to some incidental process of the court.

The SEC justifies its desire to exclude time limits from the category of "arbitrability issues" on the ground that it is necessary to minimize "mini-trials" before the main arbitration. But this concern over mini-trials seems misplaced. First of all, the parties may avoid it by changing the language of the contract (especially if they may rely on courts to look first and foremost to the language of the contract). Second, the specter of mini-trials over the issue of whether a given limitation in an arbitration agreement is "substantive" or "procedural" seems just as great as the specter of mini-trials over arbitrability. And the question of arbitrability is at least one that might have some kind of sensible answer, whereas the "substance" versus "procedure" debate is arcane and often bizarre. Finally, is the specter of mini-trials on arbitrability really more worrisome than the specter of parties being dragged before an arbitrator contrary to their expectations and expressed intentions?

Categorizations of rules as "substantive" or "procedural" should not lead one to lose sight of the language of the contract in question and the rules governing it. In this case, the wording of the rules is such that, even if a time limitation is thought of as more "procedural" than "substantive," there is no evidence that the parties intended to bring the arbitrability of timeliness issues before the arbitrators. As always, the plain meaning of the contract and the rules governing it should be the ultimate guide.

CONCLUSION

This Court should uphold its precedents honoring the contracting parties' intentions and affirm the judgment of the Court of Appeals.

Respectfully submitted,

JAMES V. DELONG
SOLVEIG SINGLETON
COMPETITIVE
ENTERPRISE INSTITUTE
1001 CONNECTICUT
AVENUE N.W.
Suite 1250
Washington, DC 20036
(202) 331-1010

C. BOYDEN GRAY
Counsel of Record
WILMER, CUTLER, & PICKERING
2445 M. Street NW
Washington, DC 20037
(202) 663-6888

Counsel for Amicus Curiae

July, 22, 2002